Compliments of the First Minneapolis Trust Company, Minneapolis, Minn.
Correspondent of The National City Bank of New York

1812

1929

Economic Conditions
Governmental Finance
United States Securities

New York, July, 1929.

General Business Conditions

THE record-breaking pace of American industry and trade has been maintained to the close of the first half year. Although a seasonable recession is looked for in the Summer, it is coming later than usual this year and confidence as to a satisfactory Autumn trade is becoming more pronounced.

New high production records for a host of major industries are indicated by the final and preliminary statistics now available covering the first six months. To date the year 1929 has apparently surpassed the corresponding period of any previous year in the output of pig iron and steel, automobiles and trucks, aeroplanes, motor boats, tires, crude petroleum and gasoline, farm implements, machine tools, electrical apparatus, copper, plate glass, sulphuric acid, silk and rayon, cotton goods, clothing, newsprint, flour, dairy and bakery products, confectionery and cigarettes, as well as numerous other less important products.

Banking and credit conditions have improved in the past two months as a result of less active security trading, combined with importations of $60,000,000 in gold, all of which served to ease the tone of the money market. Such firmness in call money as occurs the last week of June and the first of July is purely seasonal, being caused by Fourth of July currency demands, shifting of balances, calling of loans, etc., incident to disbursements of interest and dividends and redemption of bonds, to which the additional factor was added this year of subscription to several large stock issues.

Numerous other general factors in the business situation contribute to confidence for the remaining months of 1929. The marked recovery of agricultural prices from the extreme low points and the prospects for good crops, now indicate that decrease in farm purchasing power will be nowhere near so serious as was feared a short while ago. For example, the latest wheat estimate, multiplied by the prevailing price for July futures, gives a theoretical crop value not greatly below that of the previous year.

The new agreement on German reparations should have an influence of paramount importance toward stabilizing economic conditions, government finances and currencies the world over. As other countries work back to normal levels of production, consumption and prosperity, there naturally follows a continued expansion in world trade, of which the United States appears to be securing its full share.

American merchandise exports in May amounted to $387,000,000 and imports $401,000,000, resulting in an import balance for the first time in more than three years. While this is an interesting change it would be premature to attach too much significance to the figures for one month only. From the incomplete data now available it appears that the decrease was due principally to a falling off in the value of cotton exports, which were unusually heavy last Fall. Imports, on the other hand, were swelled by bringing in of unusually large amounts of sugar and other commodities in anticipation of higher tariff rates, an influence that can be only temporary. What is possibly more significant is that the total volume of trade has continued to grow and for the first five months of 1929 was 11 per cent ahead of last year, with an export balance still substantially in excess of the corresponding period of 1928.

Gain in Earnings

Corporation earnings reports that will shortly be issued covering the first half year will undoubtedly reflect the unusual activity of industry and the relative stability of commodity prices, and are expected to make a highly favorable showing even by comparison with 1928, which was the previous record year. Our tabulation of 750 first quarterly reports brought down to date shows that 375 industrial corporations had a gain of 37 per cent in net profits over the corresponding period of last year, 183 railroads gained 19 per cent and 192 public utility systems gained 16 per cent. Last year the second quarter was better than the first, nevertheless the first two quarters of 1929 will make an impressive gain, and

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should provide credits in the income accounts of scores of leading corporations sufficient to insure new high records this year, even allowing for a possible moderate recession in the remaining months. Many concerns have in six months made more profits than in the entire year 1928.

Hot weather throughout the country has resulted in brisk retail sales of Summer apparel and sports clothing as well as piece goods in silk, rayon and light weight cotton. Despite the heavy sales of textile products this year for both apparel and industrial purposes, prices of the four principal fibres have all followed a downward trend and this naturally makes it more difficult to manufacture goods at a profit. New high records in output of cotton goods have been achieved month after month, yet at the same time the margin of profit has narrowed to a point that threatens depression unless the unwarranted rate of operations is corrected.

Activity in Steel, Automobiles and Building

Steel mill operations during June kept to the high rate of previous months and averaged better than 90 per cent of rated capacity. There is still said to be a buoyant demand from the railroads, building contractors, implement manufacturers and miscellaneous consumers, and in addition to this ordinary business, the special orders arising continually from various quarters serve to preserve the backlog of unfilled tonnage. In a single week of June, for example, the "Iron Age" reported orders placed by the New York Central Railroad for 150 locomotives, also 34,000 tons by the City of New York for subways, and 8,000 tons by Russia for a tractor plant. For the first six months of 1929 steel production has run approximately 14 per cent ahead of 1928 and at the unprecedented rate of 57,000,000 tons annually. Prices are firm at slightly above last year's level, and earnings for the half year should be very satisfactory.

June was another month of large production in the automobile industry despite the fact that many manufacturers curtail operations and cut down inventory incident to preparing their mid-year financial statements, while others engage in tooling up machinery for new models to be brought out in the late Summer. Reports from the trade indicate that production in July will continue large and the establishment of a new high record in 1929 now seems assured.

Building construction, on the other hand, continues to run moderately lower than last year and statistics of total contract awards for the first six months as compiled by the F. W. Dodge Corporation are approximately 12 per cent lower than 1928 but about on a par with 1927 and 1926.

Revival of Shipbuilding

A significant factor in the general business situation is the revival of activity in American shipbuilding that is gradually getting under way and creating demands upon the steel and numerous other industries. This is the first recovery of any importance that has appeared since the war, for the shipbuilding industry has been practically dead during the past ten years on account of the surplus tonnage and depressed conditions abroad that resulted from the war.

There was a substantial boom in American shipbuilding in 1898 but thereafter the industry lost ground until 1915, when the war started a renewal of activity. By the aid of the Jones-White law passed in 1928, which provides increased compensation for carrying mails and granting of loans at low interest rates, and with the cooperation of the United States Shipping Board, contracts have been signed for the construction of more than a score of large, fast vessels calling for a very substantial expenditure.

Two of the largest liners ever built in American shipyards have already been completed for the Panama Pacific Lines (International Mercantile Marine) and a third is to be launched shortly, while other companies mentioned as either planning to build or having placed contracts include the United States Lines, American South African Line, Dollar Line, Grace Line, Munson Line, Ward Line and Export Shipping Corporation. Most of the boats will cost $6,000,000 to $8,000,00 each, and the two liners contemplated by the United States Lines will be comparable with its "Leviathan" and will involve around $25,000,000 each. Such a program will not only mean renewed activity in the yards of the three largest American builders, the Bethlehem Shipbuilding Corporation, Newport News Shipbuilding and Drydock Company and the New York Shipbuilding Corporation, but will represent a demand for labor and materials in many other industries. Ships are similar to great hotels in that they require large amounts of structural and sheet steel, pipe, cable, nonferrous metals, lumber, machinery, electrical apparatus, plumbing fixtures, hardware, paint, carpets, furniture, linen, dishes, etc.

That this program of new construction should go forward at a time when the shipping industry is still in a somewhat depressed condition may seem surprising, but experienced shipping men regard the improving conditions in world prosperity and trade as more important than the present surplus of tonnage and subnormal freight rates. It is pointed out that the profitable life of a steamship is only twenty years, on an average, and that many of the ships built during the war will soon have to be replaced. This fact, together with the time

needed to prepare specifications meeting present day requirements, to rebuild the physical plants and business organizations of the construction companies, and the large expenditures involved, are taken as proof that the present revival is not merely a "flash in the pan" but the beginning of activity that will expand and continue for several years—in accordance with the contracts now being entered into with the Shipping Board.

Agricultural Conditions

A great change has taken place in the grain markets in the past month. In the last week of May the wheat option for that month sold at 94 cents per bushel, corn at 79¼ and oats at 38¼. In the last week of June the July options sold, for wheat as high as 1.18⅛ and closed at 1.13¾, corn closed at 94¾ and oats at 43½.

We ventured last month to say that in our opinion the decline of wheat in May had been too precipitate, inasmuch as the crop was not yet made and a great part of it had two months yet to go before the weather risk was over. The month of June has seen a marked reduction in all estimates of the world wheat crop. The most sensational news was the estimate of the Canadian Cooperative authorities placing the probable yield of the western provinces at 350,000,000 to 400,000,000 bushels, as against about 500,000,000 last year. The falling off is attributed to a late Spring and general lack of moisture. Furthermore the news from our Southwest has not been so good. Threshing results have been disappointing, and rains as the grain was ready for harvest probably have done some damage. Estimates are down 15,000,000 to 25,000,000 bushels for each State. Furthermore, the Spring wheat region of the Northwest is reported to be lacking moisture in spots, which causes the trade to anticipate a substantial decline from the 322,000,000 bushels of Spring wheat produced last year.

The latest from Argentina indicates a possible reduction of 10 to 15 per cent in seeded area on account of dry weather.

There is no reason to think that the United States will not have a large wheat crop—at present the outlook appears to be for one about the size of last year's, 903,000,000 bushels, but the world crop is likely to be considerably smaller than was apprehended one month ago. It now looks as though the decline in yield would fully offset the increased carry-over, hence the recovery in price. It is noteworthy that the recovery has come at the very beginning of harvest, enabling the farmers to receive the full benefit, and refuting the oft-repeated charge that prices are regularly lowered at harvest time.

The gains in corn and oats have been due in part to the movement in wheat and in part to reports of cold and rainy weather.

The acreage in cotton is large, probably somewhat above last year's, and the stand is reported good, but the weevil menace serious. The consumption of cotton in the last year has been large enough to indicate a substantial reduction of the carry-over at the end of the crop year—July 31—and it is safe to say that a crop anywhere under 15,000,000 bales will meet with a strong market.

Hogs and cattle are bringing good prices, but the crop of Spring lambs has been large and prices rather disappointing.

On the whole the farming outlook is much better than a month ago.

Money and Banking

The money market during the past month has been treated to a spell of rather unexpected ease. At a level around 7 per cent the call loan rate has been the lowest of any time this year excepting only the seasonal low points touched in January and early February, and the month has been marked by the absence of extreme rate fluctuations such as occurred during the Spring months of the year. Although rates stiffened up late in the month to 10 per cent, this rise was not regarded unfavorably in view of the magnitude of the settlements falling due July 1. As a matter of fact an even higher level of rates at this time would have caused no great surprise.

With an easier trend in call money, time money rates have softened sympathetically, and within the past month money has been available for 90 days at 7¾ per cent, whereas a month or so ago borrowers felt themselves fortunate if they could get it at 9.

Thus far there has been little reflection of these easier conditions in the level of commercial rates. This, however, is not unusual, in view of the fact that commercial rates have had nowhere near the advance recorded in stock exchange money rates. Even at the present moderately reduced levels for the latter, it is apparent that industry and trade still have the advantage as compared with the speculative borrower, which, of course, is as it should be. Open market commercial paper continues unchanged at 6 per cent for best names. Demand for bankers acceptances has been so keen as to practically exhaust the available supply, and late in the month dealers put into effect reductions of ⅛ of 1 per cent, bringing the offering rate on 90-day bills to 5⅜ per cent.

Reduction of Speculative Activity

For the easier tone of money thus described, one apparent explanation is the pronounced

quieting down of activity in the security market during recent weeks. It would seem that the severe break in prices of a month ago, has induced a more wholesome attitude of restraint than has been evident for some months. Doubtless it is true also that apprehension of a money pinch over July 1 had not completely disappeared, and with some traders a disposition to await clearer indications as to the second half year's business trend may have been an additional factor. Whatever the explanation, trading on the Stock Exchange during June shrank to less than half the volume of active periods of the Spring.

Reflection of the reduced interest in the market appeared also in the brokers' loan figures, which for the three weeks ended June 12 showed scarcely a change at a level nearly $300,000,000 under the high point of May, and approximately half a billion dollars under the peak for all time recorded in March. During the last two weeks of June there was a recovery of $258,000,000 in these loans, but how much of this was due to re-entry of speculators into the market and how much to borrowing by corporation shareholders in connection with the huge amounts of subscription "rights" maturing within the period is impossible to say.

While it is true that these recent increases make the net reduction in loans seem rather unimpressive as an explanation of easier money, it is true also that the decline in money rates has been of very moderate character. Only by comparison with the extreme points touched during the Spring does a 7 per cent level for call money seem low. Time money at 7¾ per cent is still much the highest since 1920, barring only this year, and the Treasury in its June financing likewise had to pay the highest rate (5⅛) for any corresponding issue since 1921. In other words, what has occurred is not so much a reduction, as a stabilization, of rates, as bankers, believing that the extreme fluctuations in the call market were destructive of business confidence, have taken a hand to iron out the peaks.

Gold Movements and Foreign Exchange

The gold inflow has continued unabated, despite the lower average of our call rates. For the month of June the total receipts amounted to $26,370,000. Of this amount, the largest consignment came from the Argentine, amounting to $14,522,000 for the month and bringing the total from that country during the past four months to $29,500,000. A feature of the month was a renewal of the movement from London. After holding above the gold point for three months, sterling again weakened in June, resulting in the engagement of $14,300,000 in London for New York, of which $9,300,000 has been received and $5,000,000 is en route at this writing. These losses on the part of London to the United States, together with the fact that gold has again commenced to move from London to Berlin, have once more revived apprehensions as to the possibility of a rise in the British bank rate.

Contrasting with the position of sterling is that of the mark. Following the reduction in the Reichsbank rate from 7 to 6½ per cent in January, and during the period of reparations negotiations in March, April and May, the mark displayed acute weakness, resulting in the shipment of nearly $50,000,000 of gold from the Reichsbank's reserves to the United States. On April 25 the Reichsbank rate was raised from 6½ to 7½ per cent, and later came the reparations settlement. Responding to these two factors the mark has faced about abruptly and become the strongest of the foreign exchanges. Not only is it now at a premium as compared with dollars, but it has been strong also in terms of other exchanges.

All in all, the month's imports of gold into this country bring the net inward movement since the beginning of the year to approximately $170,000,000, an amount which but for the neutralizing policy of the Reserve banks must have exerted a marked influence upon money rates. Within a six months' period the United States has seen flow back to its shores more than a third of the gold that was redistributed to the world during the export movement of 1927-28. In the absence of a market for foreign securities in this country the world has had no other means of settling its large adverse trade balance with us than by shipping gold, which in many cases could be ill spared from bank reserves. The impairment of foreign purchasing power thus resulting is, and must continue to be until corrected, a cloud in the background of American prosperity.

Banking Conditions

In the weekly reports of member banks the principal changes of the month included an unusually large increase in so-called "commercial loans," in keeping with the exceptional activity of general business. At $9,161,000,000 on June 19, the total of these loans was nearly half a billion dollars higher than at the January low point and approximately $250,000,000 higher than a year ago at this time. The fact that this is the only important item in the bank statement which is now higher than at the beginning of the year is indicative of the extent to which the banks have favored their commercial customers during the current period of tight money.

Bank loans on securities, including loans made direct to individuals as well as loans to brokers, increased somewhat during June, but remained lower than at the March peak. Bank

investments in securities, on the other hand, continued to decline, and on June 19 were $322,000,000 lower than at the beginning of the year and $460,000,000 lower than in June of 1928.

Combining all loans and investments of these banks it appears that the total increased moderately during the month to a point within $283,000,000 of the March peak. Thus it cannot be said that the liquidation of credit has been very great. Nevertheless, the expansion has been checked, and the net result has been the establishment of something like stability in the money market around the current level of rates.

Nor does the situation at the Federal Reserve Banks suggest the likelihood of any pronounced change in the immediate money outlook. It is true that the total volume of Federal Reserve credit in use has been decreasing, but this has been chiefly due to the decline in holdings of bills bought in the open market. The volume of member bank rediscounting, which influences more directly the rates at which banks are willing to lend in the open market, has fluctuated fairly consistently between $900,000,000 and $1,000,000,000 for several months.

While flurries of tight money are to be expected at such periods as the mid-year settlements and over the July 4 holiday, these should prove temporary, as banks have indicated an intention to prevent extreme fluctuations. Aside from such periods, and barring another flare-up in the stock market, there seems no reason to expect much higher rates than now prevailing until crop moving and Fall trade requirements become insistent late in August and early in September. At the same time, with business going as strong as it is, any material lowering of the current level seems equally unlikely.

Farm Relief Legislation

The House bill for Farm Relief, embodying the provisions which President Hoover had recommended, after being relieved of the so-called debenture incumbrance which had been artfully attached to it, has finally passed both houses of Congress and become a law. It has undergone little change from the form described in our May issue, and represents a sincere attempt to deal with the "farm problem" in a practical and constitutional manner. The method adopted is that of strengthening and supporting the cooperative associations, with a view to developing some such unified control and direction of the farming business as other lines of production are supposed to maintain.

The farmers always have considered that farming was at a disadvantage as compared with the other industries by reason of the great number engaged in it and the practical difficulties attendant upon efforts to work together or have a common policy regarding production or prices. They have pointed to organized labor and the associations, "institutes," etc., existing in nearly all lines of business, and argued that their own inability to organize in like manner had resulted in an inequality of compensation which they were entitled to have corrected. In fact, however, there is much exaggeration as to the extent of control which is maintained in the other industries. Competition is irrepressible wherever industrial progress is being made, and new methods are a large factor in the present farming situation.

The purpose of the new act as set forth in section 1 is "to promote the effective merchandising of agricultural commodities in interstate and foreign commerce, so that the industry of agriculture will be placed on a basis of economic equality with other industries," etc.

In order to accomplish this purpose an extensive organization is proposed, headed by a Federal Farm Board of nine members, and including a system of Advisory Committees representing each of the farm products which in the opinion of the Board is important enough to require separate treatment, a system of Stabilization Corporations owned by the Farm Corporations, and a system of Clearing Houses, also controlled by the Farm Corporations. All of this is control machinery. At the command of the Board is the fund of $500,000,000, appropriated from the Treasury, which may be loaned for the purposes named as follows:

(1) The effective merchandising of agricultural commodities and food products thereof;
(2) the construction or acquisition by purchase or lease of physical marketing facilities for preparing, handling, storing, processing, or merchandising agricultural commodities or their food products;
(3) the formation of clearing house associations;
(4) extending membership of the co-operative association applying for the loan by educating the producers of the commodity handled by the association in the advantages of co-operative marketing of that commodity; and
(5) enabling the co-operative association applying for the loan to advance to its members a greater share of the market price of the commodity delivered to the association than is practicable under other credit facilities.

It is noteworthy that loans may be made to cooperatives for extending their membership "by educating the producers of the commodity in the advantages of cooperative marketing." It must be agreed that this is going a long way in the use of public funds.

Loans may be made to the Stabilization Corporations not only for the purchase of products from the Cooperative Associations and their members, but for trading in the market.

An Illustration

Senator Capper, one of the active sponsors of the act, has described how it is expected to

work by an illustration applied to wheat, as follows:

Briefly, here is the way the bill proposes to handle wheat, for example. The Board will ask the wheat co-operatives to name an advisory committee of seven, under regulations to be made by the Board. This committee will advise the organization by the co-operatives and recognition by the Board of a wheat stabilization corporation.

This stabilization corporation will be a central sales agency for handling wheat. It can market for its members. It can buy wheat from members or non-members. It will borrow money—perhaps a $100,000,-000 or so—from the revolving fund.

It can construct or lease elevators, sell or hold or otherwise dispose of wheat.

It is expected to announce its intention of buying a large amount of wheat. If that announcement does not bring the domestic market up to a reasonable figure, it will buy wheat. It can either market it at home or abroad. If it sells abroad at a loss, that loss will come back on the revolving fund.

The Revolving Fund for Loans Only

Senator Capper makes another statement important enough to be emphasized:

The revolving fund of $500,000,000 is placed at the disposal of the Farm Board. But except for its own administrative expenses, for which a separate fund is provided, the Federal Farm Board cannot spend any money.

The revolving fund is available for only one purpose—to be loaned. The Board can lend money to the stabilization corporations. It can lend money to co-operative marketing associations.

Success or failure of the experiment in farm relief probably will hinge largely on whether or not the stabilization corporations function. The act checks it to the farm co-operatives to make the stabilization corporations operate successfully.

The Federal Board will extend loans and advice and make rules and regulations for the stabilization corporations, but neither the Board nor the government assumes any responsibility for their operations. They are not government instrumentalities. The government lends them money but does not take stock in them.

The stabilization corporations are to be owned and operated—under supervision—by the co-operatives. These will own the stock, name their own managers and run the business.

The Scope of Possible Results

The act seems to go as far as legislation can go to overcome the handicap under which farming as an industry has been alleged to be laboring. It finally passed Congress by a practically unanimous vote and without active opposition from any source. This has been due in part to the political pledges of last year, which made some legislation of this character a practical certainty, but in a larger sense to the growth of a popular feeling that some effort should be made to deal with the so-called farm problem. When Congress does not know what to do with a problem the natural action is to create a new Commission or Board to study it. This to all practical purposes is what has been done in the present instance.

The Board should become a competent authority in the field of Agriculture, able by reason of its broad survey to give useful counsel and possibly serve as a safeguard against ill-advised agitation. It will find the best opportunity for useful activities in the field of production, rather than in the field of prices. The secret of effective price control is in regulation of production. Given over a term of years an average production of a given product no greater than the average consumption, and it would be no great problem to stabilize prices, but stabilization at what is generally accepted as a satisfactory price will almost certainly stimulate production.

If the Board, through the system of organization which is proposed, will be able to bring about a better adaptation of production to the consumptive demand, and to smooth out the fluctuations of supply by causing a withdrawal of stocks at one time and a release at another time, and can maintain these conditions and uniform prices without promoting a continuous excess of production, it will solve the problem which has defied all systems of price control in the past.

The advocates of this legislation are saying that it will give stability to agriculture as the Federal Reserve System does to the banking business, which suggests that the Federal Farm Board may well have an early conference with the Federal Reserve Board concerning the difficulties which the latter has experienced in trying to regulate the supply of credit.

The Real Cause of Low Prices

In so far as the demand for legislation was based upon erroneous beliefs concerning the actual state of the farming business and the cause of unsatisfactory prices, nothing will come of it, and there is reason to believe that to a great extent such was the case.

The real cause of unsatisfactory prices is to be found in the fact that production has been increasing faster than population while the per capita consumption of the staple food products has been declining. Dr. O. E. Baker, Senior Economist of the Bureau of Economics, Department of Agriculture, is authority for the statement that since the war, notwithstanding low prices, the increase of agricultural production has been more rapid than at any time since 1900, and this despite a decrease in the farm population and a slight decrease in crop acreage. Dr. Baker also says that the present farm population of this country is sufficient to provide for the increasing need of farm products over the next ten years.

Farm population of the United States as estimated for each year from 1922 to 1929 by the Department of Agriculture, has been as follows:

1922	30,200,000	1926	28,502,000
1923	29,800,000	1927	27,853,000
1924	29,400,000	1928	27,699,000
1925	28,981,000	1929	27,511,000

Decline from January 1, 1922 to January 1, 1929, 2,689,000.

Judging by the comments upon this population movement usually offered by the advocates of farm relief legislation, the Farm Board will be expected to accomplish a reversal, or at

least a cessation, of this movement; but what would the situation have been if this migration from the farms had not occurred and the production of the farms had been correspondingly greater? Or what if the migration had not occurred and production had been only the same as with the diminished number to be supported by the farms? Would not the situation have been worse than it is?

What will be the situation in the future if artificial prices for farm products shall cause a cessation of the migration from the farms, and improvements in methods of production continue to give an increased production per farm worker and per capita of the population?

These questions go to the heart of the problem with which the Farm Board has to deal, for the trend of production will have more influence upon the general trend of prices than all the Stabilization Corporations that can be organized, backed though they may be by the United States Treasury.

Increased Production of Wheat

It is usually instructive in such a discussion as the one over farming conditions to turn from generalities to concrete cases. Wheat is referred to more often than any other product to illustrate the need for aid, and it is interesting to note the increase of wheat production in the chief exporting countries since the period preceding the war, notwithstanding the universal complaint of low prices in recent years. The average production of wheat in the United States and Canada in the five years ended with 1913 was 887,227,000 bushels. The last three crops have been as follows: 1926, 1,238,176,000 bushels; 1927, 1,358,039,000 bushels; 1928, 1,436,321,000 bushels; average of the three years 1,344,178,000 bushels. The Southern hemisphere, mainly Argentina and Australia, produced in the years 1909-13 an average of 250,107,000 bushels and in 1928, 431,000,000 bushels.

It is interesting to examine the increase of production in this country. The States of Montana, Nebraska, Kansas, Oklahoma, Colorado and Texas had an average production in 1909-13 of 175,089,000 bushels, and in the three years 1926-28 of 373,993,000 bushels.

During these years in which Senator Capper has been sincerely and diligently laboring for relief legislation the wheat-growers of his own great and good State of Kansas have been steadily bringing more acres into the production of wheat. The average production of that State in the five years 1909-13 was 75,984,000 bushels and last year the production was 177,833,000 bushels. If production will increase at this rate under "unremunerative" prices, what will happen if prices are made remunerative?

It is probable that the development of the "combine" has had something to do with the increased production of wheat west of the Missouri River, but does not this mean that the Farm Board will have to take all of the new machinery of production into its calculations?

The Factor of Speculation

One of the avowed purposes of the new act is to reduce the amount of speculation in farm products. Probably a good deal of the speculation in farm products, as in other kinds of property, might well be dispensed with on the ground that it is uninformed and therefore not helpful, but it is by no means certain that speculation has been generally a depressing influence upon the prices of farm products. There is much more reason for the opposite opinion.

One of the most common arguments offered for some kind of control over the speculative markets has been based upon the theory that a glut of farm products occurs regularly at harvest time, enabling speculators to buy at low prices, and that subsequently prices rise regularly, enabling the speculators to sell at high prices. This is so simple a story that most people accept it at its face value, although there is an abundance of evidence to show that there is no basis in experience for it.

The idea that wheat is regularly depressed at harvest time and as regularly rises later by enough to make a profit for the speculator is not well founded.

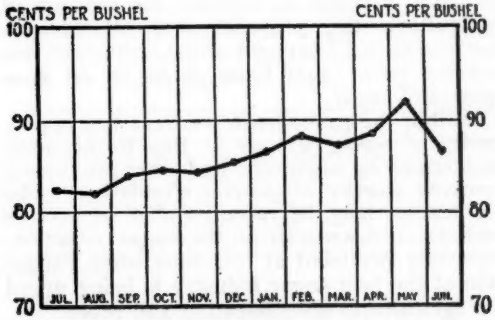
The Federal Trade Commission in its Report on the Grain Trade, 1924, Volume VI, gives the following table:

Thirty-Year Averages of Monthly Average Prices for Corresponding Months, for Wheat, Chicago, 1886-1887 to 1915-1916

(In Cents per Bushel)

July	82.69	January	86.84
August	82.44	February	88.35
September	84.21	March	87.23
October	84.83	April	88.73
November	84.60	May	92.11
December	85.67	June	86.83

The following chart illustrates these figures:



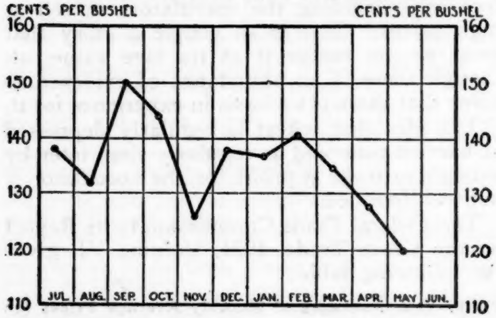
These figures are the averages of thirty Julys, thirty Augusts, thirty Septembers, etc. If there was any regular movement affording undue profits, as represented, these figures

would show it. The greatest spread is from July or August to May—nine or ten months—and in either case it is less than ten cents per bushel, which must cover all carrying charges, including warehousing, insurance, interest and risk. By May, of course, the greater part of the crop has passed into consumption.

May prices are influenced by the prospect for the coming crop. Obviously nobody knows in the Fall what the condition of the Fall-sown crop will be in the following May, and whoever carries wheat from Fall to Spring takes the risk involved in this uncertainty.

The course of wheat prices in the last year is pertinent to this discussion. The high month on the 1928 crop was September and October the next highest. The low month on the crop was May. The chart following shows the trend through the crop year from July 1, 1928 to May 31, 1929.

Monthly Average Cash Prices, No. 2 Red Winter Wheat, Chicago, July, 1928, to May, 1929.



The Sugar Tariff

Our Monthly Letter for June contained an article on the proposed increase of the customs tariff on sugar, as carried by the new tariff bill which has passed the House of Representatives and is now pending in the Senate. In that article reference was made to a calculation by members of the faculty of the University of Wisconsin showing that as a measure intended to improve the position of agriculture the proposal was ill-advised, because only 2.3 per cent of the farmers of this country grow sugar beets, while all are consumers of sugar.

Within the past month we have had opportunity of seeing a copy of this forthcoming monograph on sugar, and find other interesting contents worthy of general circulation. The publication may be recommended as a comprehensive discussion of the sugar situation, especially pertinent at this time when expansion of the beet sugar industry is being urged for agricultural diversification and relief.

Wisconsin is a State of advanced Agriculture, and the College of Agriculture of the University has been a potent factor in its agricultural development. No institution for research in the field of agriculture bears a higher reputation or has a better record of recognized achievements. The position of the State in the dairy industry has been largely due to the work of the College, and the dairy industry of the world is indebted to it for Professor Babcock's milk test.

The monograph presents the essential facts of the subject with an unbiased discussion, to which we can only briefly refer. There are several beet sugar factories in Wisconsin, but evidently the College authorities do not consider the industry to be one that affords any promise of "relief" to agriculture generally in this country. In discussing the factors which thus far have limited the development of the industry in this country it says:

The Labor Factor

The cultivation of sugar-beets involves an almost infinite amount of painstaking manual labor. The great bulk of the labor involved must be done by slow, tedious, back-breaking, hand methods. The beets must be blocked, thinned, hoed, pulled and piled, topped, and loaded into wagons by hand. Cultivation in the early part of the season, lifting the beets, and hauling to the railroad, alone can be satisfactorily accomplished by the use of horse or other tractor power.

The bulk of this hand labor cannot be done by the usual farmer and his family. Other labor must be secured; and for this purpose large numbers of immigrants are brought into a community during the beet season. In Michigan, Ohio and other central states, large numbers of Polish and Bohemian families go to the beet sections from the large cities during the beet season. Chinese, Japanese, and Mexicans are used to a large extent in the western beet regions. This type of labor often constitutes a very undesirable element in the life of the community.

These two things,—the great amount of hard, hand labor necessary, and the undesirable type of workers imported to perform the tasks, constitute drawbacks of major importance in holding down the sugar-beet acreage in the United States. The American farmer is tending more and more toward the use of large power machines in his farm operations. No satisfactory machines have yet been invented for doing the most difficult and tedious tasks connected with the production of sugar beets. And for these reasons it is unlikely that the farmers will turn to beet production in any greatly increased numbers unless the financial gains to be expected are greatly increased either by protective tariffs or improved methods of production.

The discussion points out that the farmers of this country have natural crops that are more profitable than sugar beets, and that they will not grow the latter unless subsidized to do so at the expense of the consuming population. The arguments for an increase of the present duty on sugar all say the same thing. This discussion continues:

An added factor tending to hold down the production of sugar beets especially in the central states including Michigan, Ohio, Indiana, Illinois, Wisconsin, and others is that of crop competition. Corn competes rather directly with beets, but there seems to be a comparative advantage in favor of corn. This latter crop can be grown and harvested with a minimum of hand labor, there being some kind of a machine for nearly every operation. Corn is also important in the cattle feeding industry and the dairy industry which have grown up in this region. It is very evident that beets cannot successfully compete with dairying, for example, in Wisconsin, or with cattle and hog raising in Illinois.

The total acreage devoted to sugar-beet production in the United States rarely exceeds 800,000 acres. There are approximately 190,000,000 crop acres in the seventeen states that generally grow some beets for sugar, so less than .5 per cent of the crop area in these states is now devoted to sugar-beet production. All of this vast land area is, of course, not suitable for beet production, but the agronomic possibilities for extending sugar-beet growing in these states seems very great, since there is a large acreage of suitable soils in the three regions referred to above. In any case, there certainly is a very wide margin for the further development of the sugar-beet industry in this country.

In the light of all the factors influencing the production of sugar-beets, the natural conditions of the soil and climate clearly are not the limiting factors. The limiting factors appear rather to be of an economic character. Labor supply, market price, in which the tariff is a major factor, and crop competition are among the more important factors which will tend to govern the production of sugar-beets in continental United States.

In discussing the effect of the sugar tariff upon the cost of living for the farm population the following explanation is given:

Surveys conducted by Dr. Kirkpatrick and others of the Division of Rural Life, Bureau of Agricultural Economics, indicate that the consumption of sugar is less among farm families the country over than it is among city families. There are two sets of reasons for this. In the first place, one-fourth of our sugar is consumed indirectly as confectionery, soft drinks, condensed milk, ice cream, bakery goods, canned fruits, and numerous other products. These products are used to a very much less extent by farm families than by city families. The second set of factors tending to reduce the amount of refined sugar consumed by farm families is the rather extensive use of such products as honey, sorghum syrup, and maple sugar and syrup produced on the farm.

For these reasons, the average per capita consumption of refined sugar by farm families over the period 1922-1928 will be taken as 90 pounds for the purpose of this study. Dividing the remaining refined sugar available for consumption by the urban population, we find the average per capita consumption to be 110.7 pounds, two pounds more than the figure secured when the total number of pounds of sugar consumed is simply divided by the total population.

The increased cost of sugar to all consumers and to the farmers as a group of consumers is set forth as follows:

The new tariff bill recently introduced in the House of Representatives carries a duty of 3 cents per pound on 96° sugar. This would make the Cuban rate 2.4 cents per pound since that country enjoys a 20 per cent reduction on all goods imported into the United States. This would increase the tariff on refined sugar by .68 cent per pound (from 1.8875 cent to 2.5682 cents) which added to 2.17 cents would make 2.85 cents per pound. The pyramiding of 12.13 per cent must be added; and this brings the total amount due to the tariff of 3.2 cents per pound of refined sugar. Assuming the same amount of sugar consumed as in 1928, the cost of the proposed sugar tariff to all consumers would be $400,591,625. Thus the proposed increased tariff on sugar would increase the cost to all consumers by $96,392,360.

The cost of the proposed tariff rate on sugar to the farm population would be $79,773,120 (total farm consumption 2,492,910,000 pounds) or an increased cost of $19,195,407 due to the proposed new tariff rate. Assuming, again, that the entire increased tariff rate would find its way back to the cane and beet growers of continental United States, they would benefit to the extent of $58,916,973 annually under the new tariff. But the net loss to all farmers would be $20,856,147.

It has been shown that the entire amount of the sugar tariff somewhat enhanced is passed on to the consumers and is reflected in higher retail prices for sugar. Benefits also accrue to the farmers and refiners. A small group of our farmers who produce sugar beets and sugar cane receive very material aid from the sugar tariff, but it is costing all of the farmers much more than the small group are receiving in the way of benefits. It is by no means clear that the full benefits of the tariff are finding their way back to the farmers, but is rather divided in some undetermined way between the farmers and the refiners.

The revenue aspects are commented upon as follows:

Revenue Aspects

The customs receipts from the importation of cane sugar from Cuba and other foreign countries have amounted to nearly 24 per cent of the total custom receipts of the United States. However, of the extra amount paid by consumers for sugar, due to the tariff, less than 46 per cent went to the government during the period 1923-1927, inclusive, and in 1928 less than 39 per cent of the amount paid by consumers went to the government. The revenue collected from the importation of sugar will, of course, continue to go down as an increasingly large proportion of our sugar supply is imported from our insular possessions. The cost to consumers, however, will not be reduced until a very much smaller proportion of our sugar is imported from Cuba and a correspondingly large proportion imported free of duty from our insular possessions. So long as a large part of our sugar is imported from Cuba, the price of the entire supply will be enhanced by the full amount of the Cuban tariff rate plus something in addition to cover the extra cost involved in handling the higher priced article.

However, the true cost of the tariff can hardly be completely measured in the manner outlined above. The real cost of the tariff can be measured only in terms of what is involved in denying ourselves of the bounty of nature in Cuba where conditions are practically ideal for the production of sugar. On the contrary, an unmeasured benefit of the tariff would be the satisfaction incident to the production of our own sugar supply, or at least a part of it.

Analyzing the distribution of increased cost to consumers which may be anticipated, the discussion says:

Approximately one-fifth of the entire cost to consumers is accounted for by a pyramiding of the price due to the tariff. About half of this is represented by increased handling charges between the wholesale and retail dealers, while the other half is accounted for in increases made by the importer and refiner of the raw sugar. Of the total extra cost to the consumers due to the tariff on sugar, a little more than half goes to the government and our continental producers, while the remainder goes to our insular producers and to extra handling charges due to the increased price of the article. At best, this would seem to be a rather inefficient manner in which to raise taxes or to aid our continental farmers.

The authors suggest that if it is considered desirable to aid the domestic production of sugar a large saving to consumers might be accomplished by paying a bounty of 2 cents per pound from the Treasury, as was done under the McKinley act.

As previously pointed out the cost of the present tariff on sugar was over $304,000,000 in 1928. A bounty of 2 cents per pound on all sugar domestically produced would have cost the United States government $45,881,920. In addition to this, the government would have had to forego the collection of nearly $118,000,000 custom revenues on cane sugar imported in 1928. Thus, the real cost of the bounty plan in 1928 would have been approximately $164,000,000 as opposed to a cost of a little more than $304,000,000 under the present tariff rate.

The discussion is finally summarized in six paragraphs as follows:

(1) It is physically possible to produce a great deal more sugar in continental United States. Economic factors, including our tariff policy, rather than physical factors of soil and climate, will determine the amount

of sugar produced in this country. We must determine as a national policy just how much of our sugar supply we wish to produce, and then put the tariff rate at a point that will call forth the desired production.

(2) Keen competition must be expected from our insular possessions so long as they are under the pale of our protective system. They enjoy very great advantages of soil and climate and to some extent of labor, but in some cases have the disadvantage of being a considerable distance from their market.

(3) As a farm relief measure, the present tariff on sugar is of little significance. It gives real aid to 2.3 per cent of our farmers, but it taxes all of the farmers a great deal more than the amount of the benefit to the small group. It results in a net loss to all farmers as a group.

(4) It is clearly evident that the consumer of sugar in the United States pays the tariff bill. The domestic price is raised by something more than the amount of the tariff. The foreign price of sugar was not reduced due to the tariff, as is often suggested. Furthermore, the duty-free sugar imported from our insular possessions sells at no lower price than the sugar imported and subject to the duty. For every sugar tariff dollar the consumer pays, the government gets 36 cents; our domestic producers get 14 cents; the island producers, 25 cents; and extra middleman charges account for the remaining 25 cents.

(5) This is clearly an expensive and inefficient way in which to secure revenue for running the government. It is just as expensive and inefficient as a means of giving aid to the sugar producers of this country.

(6) From the point of view of our continental producers and consumers, the bounty plan would be far more satisfactory than the present tariff arrangement. However, a bounty plan would involve greatly deflating the Islands, a consequence which warrants careful consideration.

The publication contains numerous tables giving statistics upon all phases of the subject. We gather that the average annual consumption of sugar in the United States from 1922 to 1928 inclusive was 5,427,950 tons, that the average area in sugar beets was 722,000 acres and the average production of beet sugar 872,841 tons. At this rate all around, the acreage would have to be multiplied by 6.2 in order that domestic production might completely meet the country's demand for sugar. This would give a total of about 4,476,400 acres and affords definite information as to how far sugar beets might go in solving the problem of diversification. The area required corresponds rather closely to that of the bean crop, which is 4,375,000 acres or about nine-tenths of 1 per cent of the area of cultivated lands in the country.

The Reparations Settlement

After three months of constant and arduous labor, during which the success of the conference was often in doubt, the Committee of Experts, appointed by the Reparation Commission to reexamine the reparations problem and draw up proposals for a final and complete settlement, has reported upon a new plan which has been accepted at the conference by the representatives both of Germany and of the creditor nations. The recommendations of the experts must still be accepted by the various governments concerned before the plan becomes operative, but it is inconceivable that this will not follow.

In the March issue of this Bank Letter were set forth the conditions under which the Experts' Committee met. It was pointed out that the meeting was not called because the Dawes plan had broken down or because Germany in any way had failed to discharge her full obligations under that plan. The Dawes plan was not intended to be final, and in the Dawes report was described as providing "a settlement extending in its application for a sufficient time to restore confidence," and as being so framed as to permit a final and comprehensive agreement "as soon as circumstances make this possible." With the expiration this Fall of the fifth year of the Dawes plan operation, the experimental period ends, and the time has seemed opportune for the final settlement of this problem upon which the reconstruction of Europe so largely depends.

Claims of Debtor and Creditor

Germany's first interest in coming to the council table was to have the amounts and dates of her payments definitely fixed. She wanted also to be freed from the military occupation of the Rhineland, and to be relieved of foreign supervision of her fiscal affairs. In other words, she sought the privileges enjoyed by every sovereign power of being free to solve her problems in her own way and without outside interference. At the same time she insisted that the reparations debt should be reduced to a size compatible with her capacity to pay without these extraordinary safeguards to assure payments. She protested against a reduction in the standard of living of her people below that of neighboring peoples, and urged that German industry must be permitted to grow and accumulate capital if it is to attain the productivity necessary to support the reparations burden laid upon it.

On the side of the creditors, the insistence was that Germany pay enough to cover Allied debt payments to the United States and in addition a net indemnity for reparations. Their problem was to recover as large a portion of their war costs as possible without naming a sum so great as to be beyond Germany's capacity to pay. One cardinal principle was that at least taxation upon German industry must not be reduced below the burden carried by Allied industry.

In support of their position the Germans had always the fact that they could refuse what they deemed excessive demands and fall back upon the Dawes payments, which although they might be nominally greater than those proposed, yet placed upon the Allies the responsibility of converting the mark payments into foreign currencies. To give up this transfer protection Germany insisted upon a reduction of the sums to levels which would not endanger the exchanges.

In support of the creditors' position, on the other hand, was the desire of the German people to have their obligations fixed at some definite sum. When the Dawes experts were drawing up their plan they recognized the principle adopted by the Reparation Commission, pursuant to the Versailles treaty, which holds that Germany's reparation payments should increase with an increase in her future capacity to pay. The experts recognized "both the necessity and justice" of maintaining this principle and provided "that in addition to a fixed annual payment, there should be a variable addition dependent upon a composite index figure designed to reflect Germany's increasing capacity." The experts went on to point out that it was outside their competence to "establish a limit of years or of amount for the working of the index" or "to fix the number of annuities which Germany would have to pay, as this would practically mean the fixation of a new German capital debt." Thus the Germans have not known how much they would be called upon to pay, and the desire to have this sum fixed could be counted on to act as a powerful inducement towards a settlement. Then, in addition, the natural desire of the German people to be rid of foreign domination and control was a strong influence upon the German delegation.

Thus each side had its telling bargaining points. Above all, however, was the general realization of the common good to be served by a settlement and of the necessity for concessions on both sides.

It was with these opposing interests ranged on either side that the Committee of Experts tackled in February the problem of reaching a settlement. It was confronted with three definite and concrete problems, upon the satisfactory solution of which depended the economic welfare of Europe: first, the fixing of the total amount that Germany should have to pay and the establishment of a schedule of payments; second, the formulation of a scheme for the commercialization of at least a part of the German obligations; and third, the establishment of some permanent international financial machinery to facilitate and insure German payments.

Progress of Negotiations

On April 12 the Allied experts handed to Dr. Schacht, head of the German delegation, their first memorandum of figures, calling for annuities beginning with 1,800,000,000 gold marks and rising during the first thirty-seven years to a maximum of 2,450,000,000 marks. Thence they dropped to an average of 1,782,-000,000 for the remaining twenty-two years. These combined annuities, calculated on a 5½ per cent interest basis, represent a present worth of 39,504,000,000 marks.

Despite the substantial reductions from the Dawes schedule contained in the Allied proposals, the German experts promptly rejected these figures, and on April 17 offered a counter-proposal conditioned upon certain political concessions calling for an annuity of 1,650,000,-000 marks to run for thirty-seven years only, of which the present worth was figured at about 26,000,000,000 marks or about 13,500,000,000 marks less than the Allies proposed. What this meant was a sum just enough to cover Allied indebtedness to the United States, with not a cent for reparations.

For more than two weeks the success of the conference hung by a slender thread. On May 4 Mr. Young presented a new compromise plan calling for fifty-nine annuities covering fifty-eight and a half years, comprising thirty-seven annuities of an average of 2,050,000,000 marks, and twenty-two averaging 1,530,000,000 marks. Worked out on a basis of present day value this figures to about 36,-500,000,000 marks, compared with the German offer of 26,000,000,000 marks, and the original Allied offer of 39,504,000,000.

To this proposal Dr. Schacht gave his assent subject to a number of conditions which formed the subject of the Committee's discussions during the balance of the month. By June 4 full accord had been reached, permitting the signing of the report later in the week.

The Plan of Payment

According to the Young plan, Germany is to go on paying under the Dawes plan until the end of the present Dawes plan year, that is to say, August 31, 1929. Thereafter the Young plan will become effective, and the annuities are to coincide with the German fiscal year which ends March 31.

Following is a table which shows the payments in marks for the first ten years:

Seven months, Sept. 1, 1929-March 31, 1930..	742,800,000
April 1, 1930-March 31, 1931	1,707,900,000
April 1, 1931-March 31, 1932	1,685,000,000
April 1, 1932-March 31, 1933	1,738,200,000
April 1, 1933-March 31, 1934	1,804,300,000
April 1, 1934-March 31, 1935	1,866,900,000
April 1, 1935-March 31, 1936	1,892,900,000
April 1, 1936-March 31, 1937	1,939,700,000
April 1, 1937-March 31, 1938	1,977,000,000
April 1, 1938-March 31, 1939	1,995,300,000

Thus it will be seen that the annuities proposed "start at a level which not only gives immediate and important relief to the German budget, to her exchange position, and to her need for additional internal formulation of capital as compared with the standard Dawes annuity of 2,500,000,000 gold marks, but also provides the greatest possible assurance that the new scheme will function from the beginning without any hitch or disturbance."

The system of deliveries in kind, which has played an important role in the execution of

the Dawes plan, is to be gradually done away with, and after a period of ten years all payments are to be in cash.

In considering the general schedule of payments, it is convenient to separate it into two parts, to wit, that covering the first thirty-seven years and extending up to 1965-1966, and that covering the next twenty-two years up to 1987-1988.

The First Thirty-Seven Years

As regards the first thirty-seven years, the schedule for the first ten has been given in the foregoing table, after which the annuities continue to increase gradually to a maximum of 2,428,800,000 gold marks in the thirty-seventh year. Not even at the highest point do the Young annuities reach the 2,500,000,000 standard payment of the Dawes plan. Taking the period as a whole, the average annuity will be 2,050,000,000 marks, of which 1,988,800,000 marks will be devoted to reparations and to cover the Allied debts to the United States and 61,800,000 marks to the service of the Dawes loan, which has a prior claim.

For the raising of these annuities the Young plan contemplates two sources of revenue:

1. The German Railway Company.
2. The Budget of the Reich.

Under the Dawes plan the German railways were subject to a mortgage of eleven milliard gold marks on behalf of the Allies, interest and amortization of which yielded 660,000,000 marks annually. Then, in addition, there was the transport tax yielding 290,000,000 marks, and the mortgage on German industry, interest and amortization of which amounted to 300,000,000 marks. All in all the total of these three categories footed up to 1,250,000,000 marks of the standard annuity, leaving the remaining 1,250,000,000 marks to be taken care of by the budget of the Reich.

The Young plan relieves the transport tax of any special charge on account of reparations and abolishes the mortgage on German industry. It retains as the sole contributing source outside the budget the 660,000,000 mark yield from the railways, but alters the method of its collection. Henceforward, the railway bonds are to be done away with, together with the attendant circumstances of foreign participation in the management of the railways, and there is to be substituted a direct tax imposed by German legislation and the receipts therefrom guaranteed by the German Government. The effect of these changes, combined with the reduction in the reparations total, in redistributing and lightening the burden upon the Reich is described in the report of the experts as follows:

As the amount contributed by the German Railway continues for thirty-seven years at the fixed level of 660,000,000 reichsmarks a year, the charge on the budget of the Reich varies with the total amount of the annuity. In the second year it stands at the figure of 1,136,400,000 reichsmarks and rises to a maximum of 1,768,800,000 reichsmarks in the thirty-seventh year. Thereafter the contribution from the railway company ceases, the annuity falls sharply and the budget contribution covers the whole of the German liability for the remainder of the plan.

The average increase in the budgetary contribution during the first twenty years is about 24,000,000 gold marks annually, or about .24 per cent of the total revenues of the budget of the Reich, which at present are just under 10,000,000,000. This moderate and gradual increase in the budgetary contribution under the definitive settlement plan ought to be met in ordinary years without recourse to additional taxation. Indeed, the substantial reduction of the budgetary contribution as compared with the Dawes plan makes possible an immediate resumption of the tax reduction program which has been in progress since 1924. The committee hope that such further tax reductions, coupled with a definitive reparation settlement, will give a strong stimulus to saving and thereby materially assist in the internal formation of the new capital which Germany still requires.

The Last Twenty-two Years

During the first thirty-seven years Germany finishes the job of paying to the Allies sums which the latter credit to themselves as net receipts on account of reparations, and from then on during the remaining twenty-two years the German payments coincide with Allied debt payments to the United States, plus payments to us from Germany on account of Mixed Claims amounting to 40,800,000 marks annually. As a result the annuity drops sharply from 2,428,800,000 marks to 1,607,700,000 marks in the thirty-eighth year, whence it increases gradually with the debt payments to around 1,700,000,000 marks by about the fiftieth year, and holds approximately at this figure until the final three years, when it again drops sharply to 825,100,000 marks in 1985-86, 931,400,000 in 1986-87, and 897,000,000 in 1987-88, the final year. During these last three years the payments by Great Britain on its debt to the United States will have ceased.

While Germany accepts full responsibility for the schedule set forth in the last twenty-two years, she is aided in meeting these payments by the allocation of a certain portion of the expected profits of the Bank of International Payments to a fund in which this percentage of profits shall accumulate for thirty-seven years at compound interest. It is evident, however, from the way the Plan is set up that the experts were not unmindful of the possibility that in some future reconsideration of international debts, America might find it to her advantage to forego some of her present claims, even as the Allies, as time has passed, have found it desirable to modify their original claims against Germany. The fact that the Allies did not arrange to collect any surplus for their own account after the first thirty-seven years supports this view, and a special memorandum, accompanying but not a part of the Plan, specifically provides that in the event of a reduction of the American debt, 66⅔ per cent of the fund accumulated from the Bank for

International Settlements will be allocated to Germany and 33⅓ per cent to the other countries. Certainly this is linking reparations and Allied debts with a vengeance, despite the attitude of our Government that they have no connection. So far as the last twenty-two annuities at least are concerned, it is apparent that our creditor nations have adopted the Balfour principle, which is to say that they will collect from Germany only enough to pay the United States.

Postponable and Non-Postponable Annuities

With the amounts and terms of the German debt fixed, and the raising of the funds provided for, it remained for the experts to take account of possible temporary difficulties due to causes not now foreseeable with respect to the conversion of marks into foreign currencies. It will be recalled that the Dawes plan placed this responsibility upon the Allies and set up an elaborate system of transfer control lodged in the office of the Agent General of Reparation Payments. In accordance, however, with the general purpose of relieving Germany from outside control the Young plan returns the responsibility of transfer to Germany, but provides for a partial moratorium on these payments in time of emergency.

In considering the necessity for special protective measures of this sort it will be recognized that the reduction in the size of the Young annuities as compared with the Dawes annuities, particularly over the next few years, is in itself a most important factor tending to lessen transfer difficulties. Nevertheless, the experts have not considered this a sufficient guarantee of safety, but, desirous of guarding against all contingencies, have gone further to make certain that the pressure on Germany's exchange position in any one year shall not be greater than it can bear.

Thus, it has been provided that the annuities shall be divided into two parts,—non-postponable and postponable. That part which is non-postponable comprises the 660,000,000 marks paid annually during the first thirty-seven years from the yield of the new railway tax, a figure which the Committee recognizes as very conservative, but which it favors in the belief that "it is wiser deliberately to underestimate than to run the slightest risk of weakening German credit by proposing a figure which might not command instant acceptance by well-informed public opinion." Out of this 660,000,000 marks comes the interest and amortization on the Dawes loan amounting to 61,800,000 marks annually. Here, too, lies the basis for the commercialization of part of the reparations debt, one of the most important objects before the Committee, inasmuch as it was through the promise of spot cash to be raised through sale of reparations bonds that the creditor powers consented to a reduction in the total sums due them. With this unconditioned annuity as security, it will be possible to sell these securities to private investors in the open market, from the proceeds of which the Allies will receive cash to reduce their own public debts.

The postponable annuities comprise the balance of the annual payments above 660,000,000 marks. In the event that conditions threatening to the stability of German exchange should develop, the German Government has the right, on ninety days' notice, to suspend transfers for a period not exceeding two years, during which time it will merely have to accumulate the required sums in reichsmarks at the Reichsbank for account of the Bank for International Settlements. Moreover, after one year of transfer suspension Germany has the right to suspend payments on half the postponable annuity. On the declaration of any postponement of transfer, it is the duty of the Bank for International Settlements to convene a special advisory committee, composed of representatives of the central banks of the creditor countries which shall investigate the situation and advise the Bank. Nothing in this provision, however, is to be construed as a denial of Germany's right of postponement.

The Bank for International Settlements

In foregoing paragraphs reference has already been made to this bank in connection with the raising of funds for the last twenty-two of the German annuities. The primary purpose, however, of the bank was to provide some authority of an external, financial, and non-political character in place of the present machinery and controls of the Dawes plan, including the administration of the Agent General and of various other commissioners in Berlin. It was evident early in the deliberations of the experts that some agency of the sort must be created to perform such functions as to receive the German annuities in marks, manage their conversion, and disburse them to the proper recipients, control the arrangements for the commercialization of the reparations debt, supervise deliveries in kind so long as they should continue, and to take action in connection with any request by Germany for the postponement of an annuity.

The capital of the bank is to be the equivalent of $100,000,000, one-fourth of the amount to be paid in when the bank is organized. Shares will be offered in equal amounts for public subscription in the seven countries to which the experts belong (under certain conditions shares may be offered for sale in other countries, the central banks of which approve) but will carry no voting rights, such rights being exercised by the central banks in proportion to the number of shares orig-

inally issued in their respective countries. Provision is made for the accumulation of an adequate reserve, after which earnings may be applied to dividends, which are to be 6 per cent cumulative, with the further possibility that 20 per cent of any remaining earnings may also be paid, up to a total maximum dividend of 12 per cent.

The control of the bank is to be vested in a board of directors, the members of which are to be appointed as follows:

The governor of the central bank of each of the seven countries to which members of the present experts committee belong, or his nominee, will be entitled to be a director of the bank ex officio. Each of these governors may also appoint one director, being a national of his country and representative either of finance or of industry or commerce. During the period of the German annuities the Governor of the Bank of France and the President of the Reichsbank may each appoint, if they so desire, one additional director of his own nationality, being a representative of industry or commerce. These fourteen (or as the case may be sixteen) directors will elect not more than nine additional directors from lists furnished by and which may include the governors of central banks in other participating countries.

Thus it will be seen that both debtor and creditor are represented. Inasmuch as no one holding political office is permitted to be a director at the same time, the bank, in theory at least, is subject to a minimum of political influence.

Should it be found in organizing the bank that the central bank of any country or its governor is unable to act in the capacities outlined, the Plan permits either the appointment of two nationals from that country to act as directors, or the designation of some bank or banking house to act in place of the central bank,—a provision seemingly inspired by the attitude of the United States Government in disapproving Federal Reserve participation in the Plan.

Broader Aspects of the Bank Plan

It is in its broader aspects, however, that the bank plan is most interesting. Insofar as the bank confines itself to its essential reparations functions there would seem to be slight opportunity for criticism. Its creators, however, have envisioned something beyond this, and have outlined a mechanism which is designed to be permanent, and which apparently will be in a position to perform for central banks much the same functions that they perform for banks in general. In the following words the Committee outlines what some of the principal powers will be:

(1) To buy and to sell gold coin and bullion, to earmark gold for the account of central banks and to make advances to central banks on gold as security.

(2) To buy and to sell for its own account, either with or without its endorsement, bills of exchange and other short-term obligations of prime liquidity, including checks drawn or endorsed by central banks or in respect of which three obligees are responsible.

(3) To open and maintain deposit accounts with central banks.

(4) To rediscount for central banks bills taken from their portfolios, to make loans to them on the security of such bills or to make advances to them against the pledge of other securities up to such amounts and for such period as may be approved by the board of directors.

(5) To buy and to sell for its own account intermediate or long term securities (other than shares) of a character approved by the board of directors. Its holdings of such securities at any one time shall not exceed the total of its paid-in capital and reserve funds.

(6) To invest in Germany, with the assent of the Reichsbank, reichsmark funds standing to the credit of the bank at the Reichsbank which are not transferable owing to a declaration of transfer postponement.

(7) To issue its own obligations at long or short term, secured or unsecured, for the purpose of relending to any central bank, in each case upon the specific decision of the board of directors by a two-thirds vote.

In another place of the Committee's report it is stated that,—

It is obviously desirable in the interests of obtaining results with the greatest efficiency not to limit unduly the functions of the institution. . . We consider that, by judicious, non-competitive financial development, the bank should prove a useful instrument for opening up new fields of commerce, of supply and of demand, and will thus help to solve Germany's special problem without encroaching on the activities of existing institutions.

Again, in another part of the Report, we read,—

The use of the Bank's credit by central banks within moderate limits and over short periods may, in time, become a normal function scarcely different in its exercise from the use of central bank credit by banks and bankers.

All central banks for ordinary exchange operations or for other purposes would frequently find it advantageous to make use of the facility. The second measure, that of investing within Germany some portion of the annuity receipts, should also find its uses in normal times.

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Intermediate credit operations need not be restricted, however, to any one country or to the purchase of any one country's goods. On the contrary, it would be desirable to broaden such operations in the interest of world trade to the extent that the directors of the bank approve.

As a stabilizing factor in the foreign exchanges its advantages are obvious, and if, in due time, the arrangements providing for an international settlement fund are put into effective operation, the bank should go far to eliminate the costs and risks now incurred in the shipping and reshipping of gold.

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In the natural course of development it is to be expected that the bank will, in time, become an organization, not simply, or even predominantly, concerned with the handling of reparations, but also with furnishing to the world of international commerce and finance important facilities hitherto lacking.

Especially it is to be hoped that it will become an increasingly close and valuable link in the co-operation of central banking institutions generally—a cooperation essential to the continuing stability of the world's credit structure.

Here, indeed, is a very broad program, and one which seems to bring nearer to reality the long cherished dream of a "Bank of Nations." However, while bankers fully appreciate the important possibilities that lie in the plan, they are inclined to reserve judgment as to the actual workings until they have more information than is available at the present time.

It is difficult to see how the bank can avoid competing with existing banks, and especially

those engaged in international business. It will carry deposits, upon a part of which at least interest presumably will be paid, and like any other bank it must have earnings to pay these and other expenses and make a return on its capital. Doubtless, it will seek to make itself serviceable to the banking business and avoid the competitive feature as much as possible while still accomplishing its purpose; nevertheless, it will have to be accepted as another bank specializing in international affairs. The justification for it must be found in the economies which it is able to effect.

Advantages of the Bank

There are evident reasons affording a substantial basis for the institution. As an agency for receiving and transferring the Reparations payments it will be superior to the elaborate and costly Transfer Committee of the Dawes Plan. The saving of expense of itself is an important item, and there is a possibility that the earnings of the bank will contribute something eventually to the reparations payments.

The opportunity of the bank to render useful service in transferring the reparations payments and in other ways will exist in its relations to the central banks of nearly all important countries. The experts express the opinion that it will serve as a clearing house between them and that "it should go far to eliminate the costs and risks now incurred in the shipping and reshipping of gold." There seems to be a good basis for this expectation. The bank promises to bring into closer relations, and in a degree unify, the banking systems of the world, surely a desirable tendency, inasmuch as it involves no domination, but simply more harmonious and economical operations. To a very great and useful extent the Bank of England has performed such a part in the past; but a bank in the ownership of which many countries are represented, and in the management of which not fewer than seven of the leading central banks are represented, may be considered to be more ideally constituted to play the part of Central Bank to the world than any existing institution. It remains to be seen, however, whether this is so or not. Something more than ownership and management is necessary to make a banking institution preeminent. It must be the natural center of international transactions, and time is required to establish any banking institution in that position. However, the bank will start out with a definite function, and is free to make for itself whatever place it may, within the scope of the proposed charter. There is no need now to speculate upon how large a place that will be.

Possible Dangers

Two suggestions of a critical nature have been offered, one that the bank may be politically controlled, and the other that it may be too ambitious to stabilize the finances of the world, and thus attempt tasks beyond its power—as in control over gold movements.

Both of these suggestions reduce down to the danger of mismanagement, which, of course, attends upon every proposal to establish a new institution of important powers, or in other words to improve the existing organization of affairs. It is true that central banks are more or less subject to the authority of the Governments of the countries in which they are located and under whose law they exist, but it is also true that they have more or less influence with those Governments, hence, it is possible that an institution in which numerous central banks are represented may serve as a new agency for good understanding between Governments and an influence in behalf of stable relations, commerce, cooperation and peace. The more points of contact there are between nations the less likelihood there will be of misunderstanding and a rupture of relations. Furthermore, with the central banks of numerous nations represented in the management there is little likelihood that the bank can be made to serve any political purpose.

As to the danger that the bank may interfere too readily in the adjustment of international payments, and thus prevent the wholesome check upon inflationary tendencies for which gold movements are the most effective corrective, that must be accepted as incidental to the operations of any plan for modifying the effects of credit restriction. It is true that the Federal Reserve system has almost entirely removed the danger of acute credit crises which formerly occurred in this country from time to time, and that this confidence in the banking system is to some extent misleading. Over against this danger of overconfidence must be set the advantages of a higher degree of central authority. As with all propositions of the kind it must be left to the experience and wisdom of the men to whom the management is confided. They will have to deal with the problems as they arise. In this case the management of course will be that of individuals schooled in central banking and will be in constant touch with the leading central institutions.